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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 231

HAWAIIAN GAS PRODUCTS, LIMITED, A CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 19–22) is reported at 43 B. T. A. 655. The opinion of the United States Circuit Court of Appeals for the Ninth Circuit (R. 36–40) is reported at 126 F. (2d) 4.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on February 20, 1942 (R. 41). An

order extending the time within which to file a petition for certiorari to July 18, 1942, was entered on April 28, 1942. The petition for writ of certiorari was filed on July 14, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a loss sustained as the result of the transfer of land by virtue of a condemnation proceeding was an ordinary loss deductible in full under Section 23 (f) of the Revenue Act of 1936, or a capital loss resulting from a sale or exchange of a capital asset, subject to the limitation provided in Section 117 (d).

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME.—In computing net income there shall be allowed as deductions:
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> * * * * *
>
> (f) *Losses by corporations.*—In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.
>
> * * * * *
>
> (j) *Capital losses.*—Losses from sales or exchanges of capital assets shall be allowed

only to the extent provided in section 117 (d).

* * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

* * * * *

(f) *Involuntary conversions.*—If property (as a result of its destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) is cumpulsorily or involuntarily converted into property similar or related in service or use to the property so converted, or into money which is forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, no gain or loss shall be recognized. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended.

* * * * *

SEC. 117. CAPITAL GAINS AND LOSSES.

* * * * *

(d) *Limitation on capital losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. * * *

* * * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

> ART. 117–2. *Limitations on capital gains and capital losses.*— * * *
>
> * * * * * *
>
> Section 117 (d) provides a limitation on deductions for capital losses affecting all taxpayers including corporations, that is, losses from sales or exchanges of capital assets shall be allowed as deductions only to the extent of $2,000 plus the gains from such sales and exchanges. * * *
>
> * * * * * *

STATEMENT

In 1937 petitioner, a Hawaiian corporation, held certain real estate in the Territory of Hawaii which had an adjusted cost basis of $44,979.48 (R. 19). On November 2, 1937, the Territory of Hawaii instituted an action in a Hawaiian court to acquire this property by eminent domain. Petitioner filed an answer putting the Territory of Hawaii to its proof, asserting that it did not wish to sell the real estate but that it recognized the power and capacity of the Territory to condemn it. (R. 20.)

Judgment of condemnation was entered on December 1, 1937, and the court awarded $32,500, which it found to be the value of the land, as damages to petitioner. Later in the year 1937 petitioner received the price so fixed, and title to the land was vested in the Territory of Hawaii. (R. 20.)

The Commissioner treated the loss of $12,479.48, the difference between the adjusted cost basis of the land and the amount of the award, as resulting from the sale or exchange of a capital asset and therefore limited by Section 117 (d) of the Revenue Act of 1936 to $2,000 (R. 21). The Board of Tax Appeals sustained the Commisisoner's determination (R. 22–23), and the court below affirmed the Board (R. 40–41).

ARGUMENT

The decision of the court below is correct and presents no conflict.

Petitioner owned a capital asset which was transferred to another in return for a monetary consideration, pursuant to a condemnation proceeding. The fact that the transfer was involuntary does not alter the result that there was a sale of a capital asset. *Helvering* v. *Hammel,* 311 U. S. 504, 511. If there was a transfer of property rights which can properly be classed as a "sale or exchange" then the resulting loss was a capital loss, subject to the limitations prescribed by Section 117 (d) of the Revenue Act of 1936, *supra.* Since there was a transfer of property for a fixed price in money, the court below correctly held that there was a "sale" of the property within the meaning of that statute.

Petitioner, however, urges (Pet. 5) that the decision is probably in conflict with *Helvering* v. *Flaccus Leather Co.,* 313 U. S. 247. But in that

case the property was destroyed; it was not transferred to a new owner. The Court therefore held that there was not a "sale or exchange" under Section 117 (d). The instant case presents the problem of the *Hammel* case rather than that of the *Flaccus* case, for here, as in the *Hammel* case, there was a transfer of property to a new owner.[1]

The decision below is in accord with the result, uniformly reached by the lower courts, that gains or losses realized in condemnation proceedings are subject to the provisions of Section 117 (d). *Commissioner* v. *Kieselbach*, 127 F. (2d) 359, 360–361 (C. C. A. 3), pending on petition for certiorari in respect of other points, No. 184, this Term.[2]

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[1] In the *Flaccus* opinion the Court ruled that the result was unaffected by Section 112 (f) which merely provided for non-recognition of gains or loss on certain involuntary conversions of property. Section 112 (f) did not in any way deal with the question whether such gain or loss was to be classified as ordinary or capital. The Court did not rule that none of the involuntary conversions listed in Section 112 (f) could be classified as sales or exchanges under Section 117 (d); it simply ruled that Section 112 (f) had no bearing upon the classification of capital gains or losses under Section 117 (d).

[2] The issue, as far as here relevant, presented by the petition for certiorari in the *Kieselbach* case is whether the interest awarded in a condemnation proceeding is taxable as ordinary income or as capital gain. This also was the issue litigated in *Seaside Improvement Co.* v. *Commissioner*, 105 F. (2d) 990 (C. C. A. 2), certiorari denied, 308 U. S. 618; and in *Commissioner* v. *Appleby's Estate*, 123 F. (2d) 700 (C. C. A. 2). It appears to be implicit in these two cases that, whatever the taxability of the interest, the gain involved in the award itself is a capital gain and not ordinary income.

CONCLUSION

The decision below is correct and there is no conflict of authorities. The petition should be denied.

Respectfully submitted,

OSCAR COX,
Acting Solicitor General.
SAMUEL O. CLARK, JR.,
Assistant Attorney General.
SEWALL KEY,
GERALD L. WALLACE,
JOSEPH M. JONES,
Special Assistants to the Attorney General.

JULY, 1942.

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